RICHARD RUSSELL'S DOW THEORY LETTERS INCORPORATED

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July 21, 1993 **LETTER 1126**

OVERVIEW: (1) My friend Gary Shilling runs a private investment fund (see *WSJ* July 12). The fund is up over 100% this year. Gary did it by betting that the Kondratieff or "Long Wave" was heading down and that the US, Europe and Japan are all in the grip of deflation. Thus, Gary bet on lower oil (boy, was he right, with oil at a current three year low), still lower real estate prices, tough world competition (especially from Asia), and lower interest rates (thus higher bond prices). Gary is long the dollar on the basis that "we're the best of a bad lot." When a guy's fund is up 100%, you've got to take what he says seriously.

(2) Congress is meeting in an attempt to put what's left of the Clinton budget together. But there's a problem. There probably aren't a dozen people in Washington who believe that the Clinton program will either lower the deficit or be good for business. In a phrase, the Clinton so-called "Deficit Reduction Program" is a disaster, and if it passes it will be the Democrat's disaster. Yet, if the program doesn't pass, what's left of the Clinton presidency? . . . Sensing all of Clinton's problems, Saddam Hussein has gone back to playing, "Drop dead, USA." What will Clinton say? What will he do? Darned if I know -- hey, you voted for him, I didn't.

(3) Meanwhile, the G-7 people met, and not a whole lot was accomplished there either (although Clinton claims otherwise). I did note, however, that immediately after the meeting the German stock market broke out to a new high for the year, and German bonds surged higher. If the German stock market, in the face of the sick German economy, can surge to new highs, it's telling me something. It's telling me that in the face of chronic world recession and unemployment: (a) global interest rates are heading lower, (b) central banks will be pumping up their respective money supplies, (c) the governments of the world are anxious to reflate, (d) and if inflation starts heating up again, well that's the price you pay when you play the "jump start the economy" game.

THE MARKET PICTURE: My Primary Trend Index (PTI) and the advance-decline ratio both hit new highs on July 8 and again on July 12. That's pure market action, and it's impressive.

There are two ways of looking at any market. One way is via your personal opinion -- what you think, your instincts, your knowledge, your conclusions.

You all know my opinion, which is that this is the most expensive stock market in history. Furthermore, this market has remained expensive for over two years, the longest "expensive market period" on record. The main reason for market strength is enormous public buying of mutual funds plus extremely low interest rates. For these reasons I have to conclude that this is also a dangerous market.

But let's face it, experience has a lot to do with the way I think. I've been watching markets for a long time -- roughly 45 years. Maybe I've seen too many bear markets. Maybe I've seen too many plans go astray. Maybe I've seen too many market geniuses hit the skids. In other words, maybe I'm just prejudiced against severely overpriced markets.

The other way of dealing with the markets is by examining what the market is actually doing. Forget the news, forget your personal opinions, just deal with what the market itself is telling you. Deal with the price action, the movement of the averages, the A-D ratio,

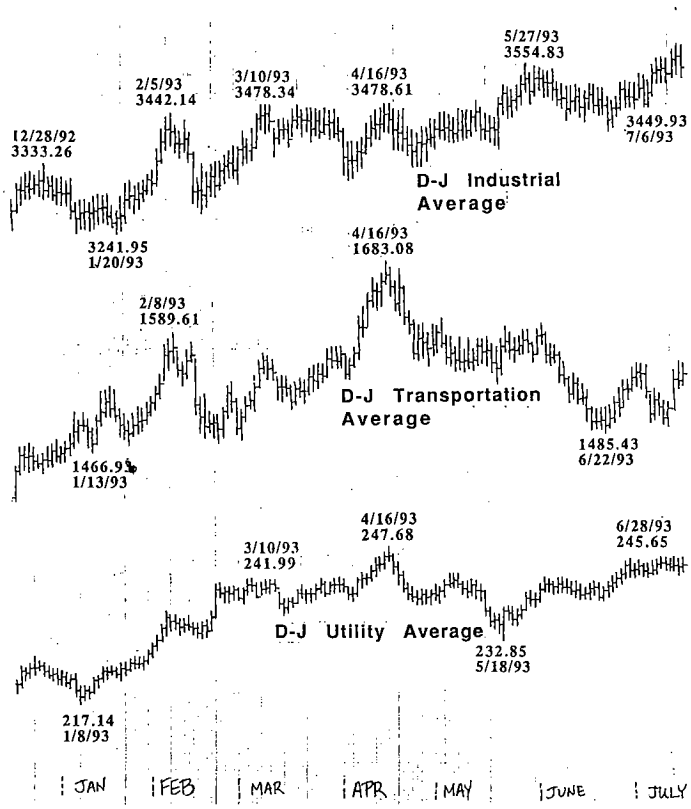
July 9 DJIA 3521.06; PTI 3858; A-D Ratio -4.13
July 16 DJIA 3528.29; PTI 3866; A-D Ratio -3.96
Dow Yield: 3.12%; Dow Price/Earnings: 32.1
Dow 200-day MA: 3368; Dow 30-day MA: 3507
Dow Times Book Value: 2.71; PTI 89-day MA: 3809
Percentage of Undervalued Blue-chips: 7%
Low Risk Buy Index: +60

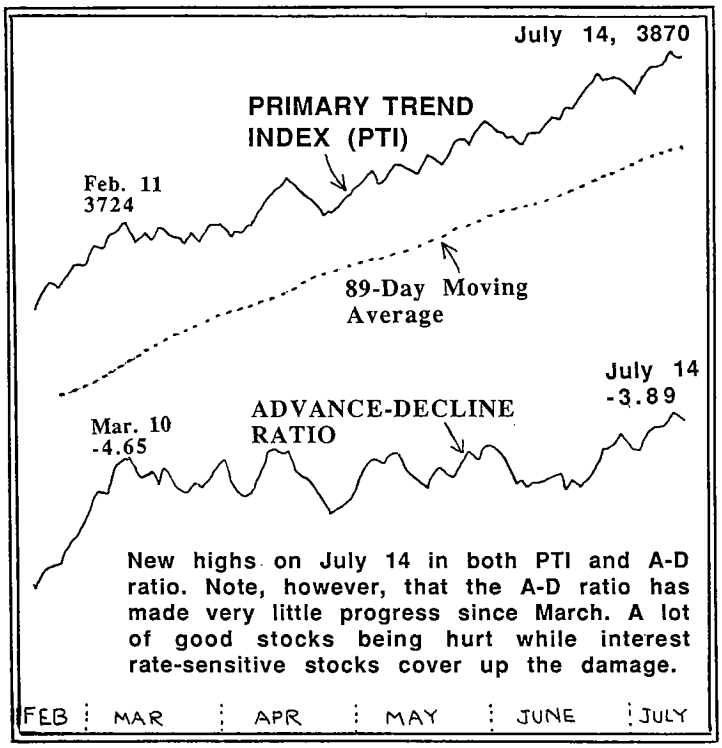
the PTI -- on the thesis (adhered to by all true technicians) that the market is its own best forecaster. The story here is that so far, from a price action standpoint, from a Dow Theory standpoint, the main trend of the stock market is still -- UP.

The fact is that even with divergence on the part of the Transports, the Dow has shown no signs of confirming on the downside. My PTI, which tracks the hidden undercurrent of the market, continues to hit new highs. The advance-decline ratio breaks out on the upside (and yes, I'm well aware that 38% of all the stocks on the NYSE are extremely interest rate sensitive). Finally, the short interest keeps pushing to new record highs. Consequently, there's still plenty of skepticism on Wall Street (which is exactly what the bulls want).

So should I play guru? Better not. Better to simply tell my subscribers the whole story without hopes and wishes and trimmings. I wish I had a crystal ball. I wish I could say, "Hey, this bull market is ridiculously expensive, and on September 3 (just as it did on September 3, 1929), the Dow will hit its all time high. So beware, that will be the final high. That will be your last chance to get out before a disastrous five-year bear market hits."

I wish I could pin-point it like that. But I'd be an absolute charlatan if I even tried. You see, it can't be done (although God knows, a lot of advisories do try).




July 14, 3870
PRIMARY TREND INDEX (PTI)
Feb. 11 3724
89-Day Moving Average
July 14 -3.89
ADVANCE-DECLINE RATIO
Mar. 10 -4.65
New highs on July 14 in both PTI and A-D ratio. Note, however, that the A-D ratio has made very little progress since March. A lot of good stocks being hurt while interest rate-sensitive stocks cover up the damage.
FEB
MAR
APR
MAY
JUNE
JULY

So what do I do? I tell my subscribers that this is a very expensive market, that based on past experience, this is the time to protect your assets rather than add more equities to your portfolio. I tell my subscribers that based on history, this bull market is living on borrowed time. Furthermore, the LONGER this market remains in the overvalued zone (which means the greater the period informed investors have to distribute their stocks), the worse the ensuing bear market will be.

But I also tell my subscribers that based on the actual evidence at the time of this writing, the end is not here yet. The price action is just not telling me that Wall Street is ready for the big bust. Not yet, it isn't.

BEING MORE SPECIFIC: In the last Letter I pointed out that the Dow had refused to confirm the weakness in the Transports. The new first downside level of importance for the Dow is **3450 level.** The Dow should hold above that level. If the Dow does fall below 3450, it will have broken below its last two decline lows, and it will have reversed a rising trendline that has held since the beginning of the year.

Currently I'm receiving a rash of anguished letters from subscribers. They all want to know, "What's the market going to do?" Patience, patience. The market is a law unto itself. It will remain bullish as long as it wants to, and it will only turn bearish when it's ready to. This is probably a good time to repeat that old Wall Street adage which states, *"The market always does what it's supposed to -- but never when."*

In the final analysis, our job is to stay firmly rooted in reality and to abstain from hopes and wishes and fantasies. The market doesn't follow us, but we sure as hell better learn to follow the market. To do otherwise is the guaranteed path to patched pants and thin wallets.

Comment: In his latest report, Jim Grant (*Grant's Interest Rate Observer*, 30 Wall St., NYC 10005) notes that *"At current rates of acquisition, the Federal Reserve is unlikely to run out of government securities. Bills, notes and bonds bought outright for the system's account grew at an 18.2% rate over the past three months and at a 13.75% rate over the past year . . . The Fed continues to expand its balance sheet faster than the commercial banking system is expanding its collective balance sheet."* Meaning, that the Fed is "pumping up the monetary volume" at a furious rate, even while they mouth worries about inflation. Moral of the story: It ain't what they say, it's what they do.

INVESTMENT POSITION: Bearish subscribers call here wanting to know whether the PTI has turned down. I tell them, "Well I tried pushing it down, but darned if it doesn't just keep advancing to new highs." Since the PTI seems to have an excellent handle on the stock market, I continue to rate the market as bullish. Now you know why the bull remains in the box.

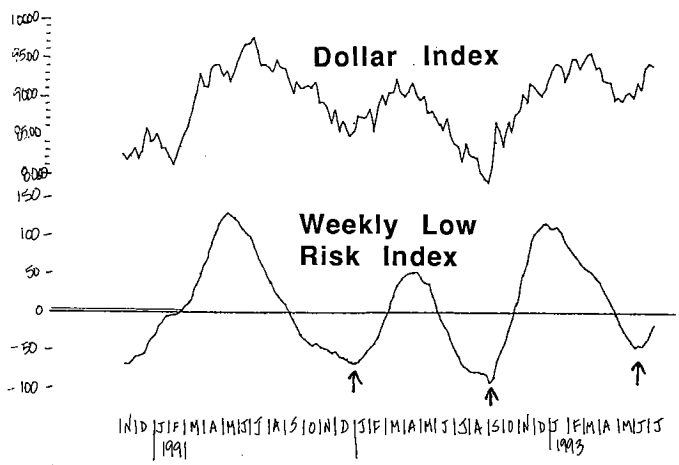
Subscribers keep asking me about the Low Risk Index. The figures for my Low Risk Index (LRI) appear on page 1 of each Letter. Those are the figures for the Dow alone. But I run the LRI on a number of different items including stock groups. As older subscribers know, when the LRI drops below zero and then turns up, that signals a cessation of downside momentum and therefore an advantageous entry point.

Last week two stock groups turned up from below zero, **Money Center Banks** and **Electric Utilities**. Note that both of these groups are interest rate-sensitive. In order of strength, the leaders in Banks are Citicorp, Bank of NY, Bankers Trust, Chemical Bank, Republic of NY. As for the Electrics, they are, in order of strength, Gen. Pub. Utilities, Consolidated Edison, Niagara Mohawk, Amer. Elect. Power, Phila. Elect., Duke Power, Central and SW. All yield over 5%.

As for the gold stocks, in order of strength they are American Barrick, Placer Dome, Pegasus Gold (Amex), Echo Bay Mines (Amex), Homestake.

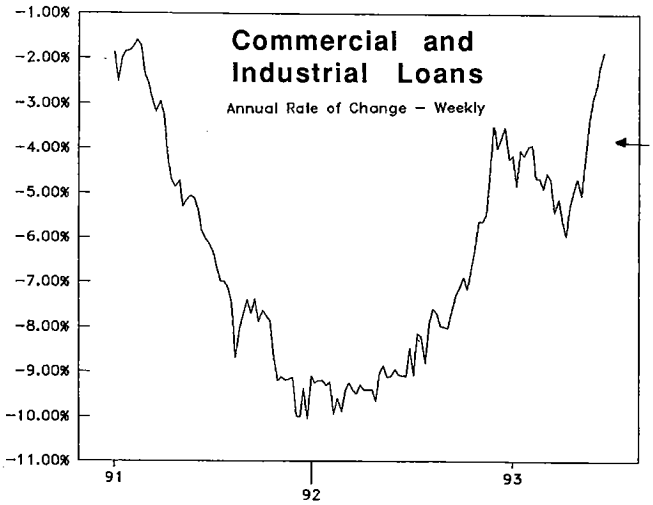
Maybe I'm wrong, but I took profits on most of my Hong Kong stocks. Hang Seng Bank was the winner, by far, but almost all were on the profit side of the ledger. You might at least think about doing the same (China is clamping down due to tremendous overheating and rampant inflation). Ah, the real reason I sold -- I feel more cautious than greedy these days. Actually, I feel this way about ALL stocks (not including the golds of course). And I'm perfectly willing to be wrong (or should I say, "right too soon").

ODDS & ENDS: We run the Low Risk Index on all the currencies as well as on stock groups. This is a chart of the Dollar (weekly) with the LRI. Note that the Dollar Index has turned up from below zero, a decided positive for the buck. You can't use this information for day to day trading, but it does tell us that the intermediate trend of the dollar is UP, regardless of daily or even weekly pops in the other currencies.

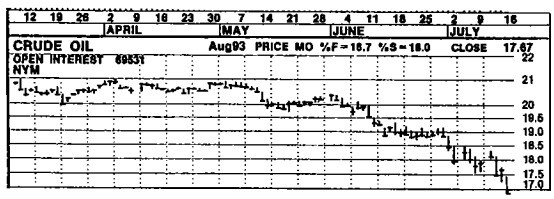


One powerful consideration regarding the relative strength of currencies is how the nation's economy is doing. This chart shows a problem area for the US which is finally improving. The rate of

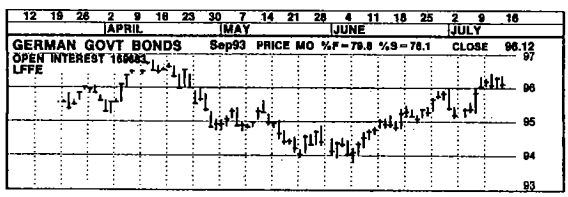
change in Commercial and Industrial loans is now spurting higher, suggesting a forthcoming noticeable pickup in the economy. Clinton and the Fed will breathe easier if this continues.



From its high of over 21 dollars a barrel set in March, Crude Oil has slumped below 17 on the Aug. contract. It's probably due for a bounce now, but the decline in crude is a deflationary indication. Of course, Japan loves low oil prices since they have to import all their oil. And Japan pays for their oil (as does everyone else) in dollars. Therefore, a cheap dollar (and a higher yen) may push up Japanese export prices, but it greatly reduces their fuel and energy costs.



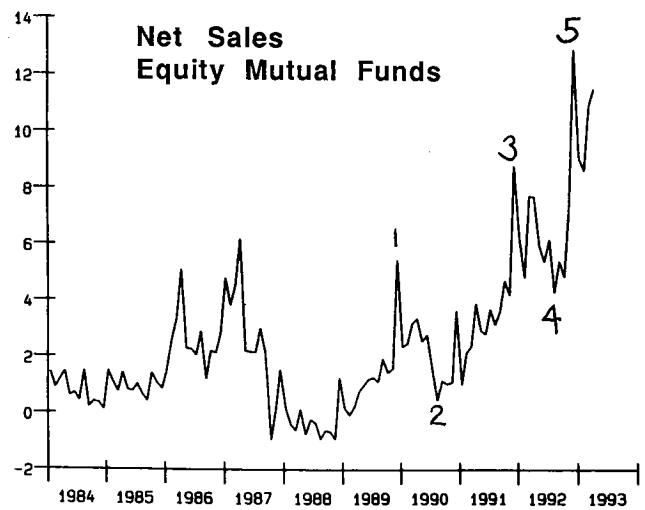
A lot of my subscribers own German bonds, both as an alternative to dollar bonds and as a good source of income. With German interest rates now coming down, the bonds are acting well. The only problem, of course is the problem of the D-mark vs. the dollar. Nobody in the world knows where the D-mark will be vs. the dollar a year or even six months from now. But I continue to believe that German bonds have a place in diversified portfolios (chart of the bunds and oil courtesy of *Investor's Business Daily*).



THE FUNDS: Wall Street is famous for giving the public what it wants. In a bull market (as now) the public wants stocks, and Wall Street is only too willing to oblige. In a bear market the public wants out of stocks and into cash, and Wall Street willingly buys back its product (at a substantial discount, of course).

I tend to think of Wall Street as one great, obliging mother. During good times she would send her children (stocks) out into the world to seek their fortune. In bad times, the children would always come home to mother.

The Wall Street phenomenon of the '80 and '90s is the fantastic proliferation of mutual funds. Consider this -- since 1990 the industry has added 1000 new mutual funds. This is more than a third of what existed three years ago. Not to be left out of the bonanza, the banks have rushed into the picture. By the middle of 1992, 14% of all long-term fund sales and 33% of money market mutual fund sales were being brought out by the banks.



The next step -- funds being sold in strange places like department stores, supermarkets and on Home Shopping Networks or on the QVC network.

So far, there has been a 27% penetration of households by the funds. In other words, one out of every four households in the nation owns one or more funds. The target for the industry -- increase penetration. During the Great Depression Hoover promised "a chicken in every pot." Today the industry dreams of "a fund in every home."

What are the implications? To Richard Russell, the implications are ominous. I believe the funds are fostering a false sense of security among the public. The public feels that "the stock market over time can only go higher," and "my fund is being run by professionals who know what they're doing."

Ah yes, but remember, a bull market makes heroes out of most advisors and fund managers. But the other side of the coin is that a bear market turns these same advisors and managers into taxi drivers and waiters.

Forgetting sarcasm and cynicism, the real problem is that somewhere ahead lies a major bear market. When the bear market hits it will play hell with the funds. They will be decimated. And the public, which is now so heavily in funds, will be hurt, both financially and psychologically. At that time, all the worries that are now lesser worries in the public's mind will become big worries, and I mean major worries (i.e., unemployment, the deficits, international competition, the influx of foreigners, crime, poverty, etc.).

I thought the accompanying chart (courtesy of Ed Hyman at *Int. Strategy and Investment Group* in NYC) was very interesting. Here we have a chart tracing net sales of equity mutual funds, and as you can see, sales have exploded.

I haven't talked about Elliot waves in a long time, but it seems to me we have a clear five waves up on the chart. The rise also has a parabolic look. Is fund buying in the process of topping out? The chart makes me wonder.

NOTES & QUOTES: In his latest FAX here, *Sindlinger* notes that the number of US households owning stocks or mutual funds has risen to 57 million, "the highest level in history." Russell comment: That's great for Wall Street now, but it will play hell when the next primary bear market hits.

* *

Industry layoffs continue. Ed Hyman of *ISI* (Ed keeps careful track) says, "For the month of June we counted 40 layoff announcements vs. only 19 for June last year. This doesn't necessarily mean that the economy is getting weaker, but it does argue that it is not getting stronger and that downward pressure on wage gains is persisting."

* *

The US imported 9.2% more oil this year as US oil production dropped to a 35-year low! The US pays for all its imported oil in dollars, and I predict that at some point the Arabs are going to want gold and dollars; it's only a matter of time. It will happen when the dollar takes its next swan dive.

* *

My how things change. A month ago the French franc was the hot currency, and the talk was that maybe it would take over from the D-mark as THE currency of Europe. Then weakness hit the franc, and it dropped precipitously against the D-mark. The latest rumor is that the French might even devalue the franc and drop out of the ERM. One reason, unemployment in France is running around 11%, and the French don't want to be ruled by Bundesbank stringency.

* *

I've said that the crisis of the '90s is going to be global unemployment. But wait -- there's a variation. The United Nations Population Fund said last week that people are moving across international borders in unprecedented numbers, and they warned that this massive migration "could be the human crisis of our age." Yes, and all these people are going to want jobs.

* *

Talked to an import-export guy last night. He travels to Tokyo once a month. Told me he has "a small office" in downtown Tokyo. Rent -- $10,000 a month. Remind me not to take a vacation in Japan this year.

* *

Words, words: *"The battle for inflation is never over and the very minute a society declares victory in that battle is likely to be the very minute the seeds of the next round of inflation are sown, with all their painful and inevitable consequences for the future."* E. Gerald Corrigan, outgoing president of the Federal Reserve bank of NY. Russell comment: Gee, if that's what he really thinks, no wonder he's leaving.

* *

The results of the big 1990 Budget Deal are coming in and -- surprise, although "the rich" had their taxes raised, they paid less of the total by 6.1%. And the average Joe, he paid a larger percentage of the total. Harvard economist Martin Feldstein says, "The evidence is strong that in 1991 they picked up rates at the top and revenue fell. This should make Democrats question the idea that the tax rates they are talking about will raise the revenue they expect." Writes Paul Gigot in the July 9 *WSJ*, "The Clinton Administration knows all about this, but wants it kept quiet until the tax bill passes. Treasury economist Alicia Munnell is in denial, even though her staff knows that Feldstein is right . . . Other Democrats don't even want to hear about it. That's because for them, taxing 'the rich' is about class warfare politics, not about revenue. It's about having a foil to run against."

* *

Fortune magazine (July 26) under an article titled, "Deficit Cutting, the Great Fraud," notes that "even if Clinton's plan cuts $20 billion from the budget next year, spending still *rises* by $38 billion."

* *

Roughly 53% of the total US work force is employed by small business. Furthermore, 80% of US businesses pay taxes at the individual rather than the corporate rate. But wait, there's a bit of a problem. A very high percentage of small businesses are either Subchapter S set-ups or individual proprietorships. As such, the new Clinton sky-high tax boosts will hit small business hard. Under a barrage of protests from small business owners two weeks ago, Clinton replied, "Unless we are firmly committed to small business growth, we cannot succeed as a country." Right, tell us about it, prez. Said the President of the National Association of Manufacturers, "Crazy as it sounds, many small businesses will pay a higher effective tax rate than *Fortune's* 500 corporations." Russell comment: Yeah, it's crazy, all right. The new rate for individuals will rise from the current 31% to almost 40% at the top bracket." And then you add state taxes, mmm.

* *

IBM -- the rumor is that on July 27 IBM might announce that it's cutting its current $2.16 annual dividend to $1.00. That's one buck. How the mighty have fallen. The stock, 175 at its 1987 high, has sunk to the 46-47 level, a loss of better than two-thirds of its peak value.

* *

Canada is in the throes of the biggest land and mining fever since the gold explosion of the '80s. But this time it's diamonds. Millions of shares in diamond mining companies are traded daily in Canada, and it is estimated that this has added $2 billion in value to these shares over the last 18 months.

* *

Speaking of diamonds, like gold they are hot-hot today. The Central Selling Organization (owned by DeBeers, which controls 80% of the world's diamonds) said last week that diamond sales hit a record $2.54 billion in the first six months of 1993. You know, somebody out there is socking away a lot of gold and gems. As I've been saying, the BIG PICTURE today is a quiet yet persistent move OUT of financial assets and into tangible (real) assets. In other words, ladies, don't sell your diamond rings or ruby ear rings or your Rolex watches yet.

* *

One item I find particularly annoying is the widespread talk of Clinton's "$500 billion reduction in the federal debt" over the next five years. The fact is that under Clinton the national debt will rise by at least one trillion dollars before his first term is over. Clinton's so-called reduction is, in reality, a reduction in the RATE OF INCREASE in the national debt. Why don't reporters get it straight and why don't they tell it straight? I really feel that it's rotten journalism.

* *

Which reminds me, another pet peeve of mine is reporters and even editors of publications who have no knowledge of markets or finance calling here and questioning me or even interviewing me about the markets. I don't know whether it's the publication's fault in sending out business-ignorant reporters or whether it's the reporters' fault in not learning anything about the subject they're dealing with. Seriously, I've talked to reporters from major newspapers who don't have a clue about their subject. Talking to them is like talking to a blank wall but a lot more frustrating.

* *

Is there big money to be made on Wall Street? You better believe it -- particularly if you're one of the brass at the Street's most profitable investment banking firm, Goldman Sachs & Co. In 1992 Goldman had a pretax profit of $1.4 billion. The firm's 142 partners split at least $1.02 billion among themselves after Sumitomo Bank, itself a partner, took 12.5%. Former Goldman Chairman Rubin and current Chairman Friedman took $53 million between them. *Financial World* lists at least 19 Goldman partners who each took in $15 million or more. Then there are a lot of other lesser partners. There's nothing like the money business in a big bull market.

* *

Speaking of big money, Merrill Lynch has $500 billion under management. That's 2.5% of all the private funds in the nation. Speaking of Merrill, the brokerage stocks are probably as good a leading indicator group of stocks as any. And Merrill is the key. When Merrill (MER) tops out, this bull market will probably be over. On my monthly chart, a break below 60 would spell "finis" for Merrill. At 60 Merrill's 1991-93 rising trendline would be broken.

As an added comment on the above, many years ago my wise old father told me, "Dick, I don't know if you're interested in making real money. But if you are, you should consider going into the money business. It's one of the best businesses I know of. It's international, it's fascinating, you have no inventory, and if you make a mistake you can get rid of it with a 10-second phone call." That proved to be good advice.

* *

Funny, where you can read interesting items. This is from the current issue of *Playboy:* "Leave it to the Swiss to keep their money as well scrubbed as their picture-postcard towns. The Swiss National Bank spends a lot of money replacing up to one-third of its bank notes each year -- yanking dirty besmirched or torn francs before they soil the national pride. According to the chief cashier of the central bank, 'The first thing you see when you arrive in the

country is the money. It's like a national identity.'" Question: Russell, do you get *Playboy?* Answer: Yes, I like the interviews.

* *

Nightmare: My mother, born in NYC, once told me that the first thing that struck her when she met my father (he was a WWI Naval lieutenant at the time) was that he had grown up in the South (Orangeburg and Charleston, South Carolina), but that he was not prejudiced against blacks. Some years later (coming back from a jazz jam session in Harlem) I was held up at knife point by a group of blacks. I broke away and probably shattered the world's record (I was a top sprinter at the time) in a dash to the 125th Street subway (NYC was the city).

The scene changes to 1989 in San Francisco (I had given a speech there). I left my hotel room at 5AM next morning looking for a *NY Times*. I made the mistake of turning up a side street off Market. Halfway up the street (it was still dark) I got jumped by two large black men, and unfortunately, I was no longer a sprinter. Net result: I lost a wallet with three bucks in it, my driver's license, my credit cards -- and I gained one large black eye.

Nevertheless, like my father, I bear no prejudice. But I also have a hobby -- it's called "Surviving." Chuck Norris, the former world Karate champ, tells us that "The best defense is not to offend." I learned that lesson long ago, but I've also learned, finally, to be a lot more careful about where I wander at night (and now even during the day).

Which leads me to this -- one of the massive problems of today (and it's going to be A LOT WORSE tomorrow) is the problem of the huge underclasses in America. Go to any city in the nation and hit the ghetto districts and you'll get a good working knowledge of what I mean (that's assuming you have the nerve to even get near the ghetto districts).

As far as the blacks are concerned, I view their plight partly as the product of 200 years of prejudice. The blacks have endured insults, slights, put-downs, injustices that no man or woman should ever have to take. The result -- a sub-nation isolated in ghettos, largely unemployed, angry, uneducated, armed and on the loose. The blacks, brought here originally as slaves, are the only ethnic group that have been totally cut off from their roots. Named after white families who owned them, even their original family names have been lost to them.

But forget what I've written above. You want to know what it's really like in the black ghetto of today? You want a mind-numbing insight? Two black 21-year old twins have produced a remarkable film called "Menace II Society." It's one of the toughest, meanest, scariest films I've ever seen. If you want to see the problem of the black underclass, if you want an insight into the mentality and actions of the gangs that now infest (menace is the word) almost every city in the nation -- then go see Menace II Society. My son, Ryan, and I saw it in a theater that was 90% black. The most frightening part of the whole experience was that the black teenagers laughed during many of the most brutal scenes. Believe me, if you could laugh at that movie, you could laugh at death itself. And they do.

And as a final aside, this film underlines what I've been saying in the last few Letters, the problem today (and worse tomorrow) is -- no jobs, pink slips, businesses that are run by computers with very few people. Some people call it improving corporate productivity. Others call it UNEMPLOYMENT. Unemployment will be "The Nightmare of the Nineties." I think it already is.

* *

Faye and I just saw the new Clint Eastwood film, "In the Line of Fire." It's a winner. Clint is terrific and John Malkovich comes across as one of the best, weirdest and most fascinating villains of all time. Actually, I thought Malkovich made the movie.

* *

Survival: Who are the world's premier survivalists? The insects, hands down. With over a million species of insects and more being discovered almost weekly, no single species of insect has ever been eliminated. They're all here, every last one of them.

* *

On another subject, America's favorite dessert (surprise) is ice cream. More than 200 ice cream manufacturers compete for an incredible $10 billion in annual sales of ice cream. Ice cream is my own favorite dessert, but I don't eat it anymore. Ice cream is loaded with salt and fat, two items I try to avoid. My substitute is no-fat yogurt, which still has a lot of calories, but at least it hasn't got the fat of ice cream. When I was younger back in NYC, my favorite of all foods was the great hot fudge sundae made by Schraft's. That chocolate ice cream was unbelievable as was their hot fudge. And all for 35 cents! Of course, 35 cents was real money in those days of nickel newspapers and penny post cards.

* *

With gold in a bull market, there is talk of a revival in the market for collectibles (gad, maybe even the collapsed stamp market will come back to life). Speaking of collectibles, Edgar Allan Poe (1809-1949) published his first work, *Tamerlane and Other Poems,* in 1827 at the tender age of 18. Poe paid for the work himself, and he published only 50 copies. Only 12 copies survive today. This makes it the rarest and most expensive of all American first editions. Now there's a collectible.

* *

On a related subject, at a recent auction two splinters from the cross of Jesus were sold for a total of $18,500. Based on that price, one analyst figured that the total value of the cross would come in at $50 billion.

* *

Aw, I can't get away with anything. A few Letters back I called George Soros Henry Soros. Why did I do it? Two reasons. I wanted to see whether my subscribers were "on the ball" and watching for mistakes. And I just wanted to annoy George (he's making too much money anyway). I received about 15 letters correcting me. So it's obvious that my subscribers are extremely alert. But strange, I haven't heard a word from Soros yet.

Then in the last Letter I referred to a gold chart, but darned if I didn't forget to include the chart. Am I "losing it?" I'll have to get to bed earlier.

* *

Every few days I get a big envelope telling me, "Congratulations, You've Just Won Ten Million Dollars in Our Contest." Time Life does it, Publishers Clearing House does it, other outfits do it. Can these outfits get away with this kind of rubbish? I guess they can, because there's always a lot of small print stuff which negates the big headlines. Spare me, Time Life, I'm not interested.

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This country is going nuts over gambling. The big $110 million 14-state "Powerball" contest a few weeks ago had poor fools standing in long lines to buy tickets. The odds on winning were 58 million-to-one, but that didn't stop thousands of people from spending their money in the hopes of winning that $110 million. Hope springs eternal and a lot of people seems to live on hope. Consider this: if you bought one million tickets (one dollar each) in an effort to win Powerball, the odds would still be 58-to-one on your winning. I wouldn't take those odds in any casino, would you? Yet millions of people willingly spend their money on odds of 58 million-to-one. Pathetic.

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Playing at the Sahara Club in Las Vegas is Cook E. Jarr and the Krums (he's been voted number one lounge performer in Vegas for the past nine years). I haven't heard of a group with a name like this since San Francisco about a decade ago when there was a group (honest) called Dow Jones and the Averages (I think they disbanded with the '87 stock market crash).

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The Chinese boom goes on. Beijing announced that foreign companies in '93 will sign contracts with Chinese partners to the tune of $80 billion. China, which now faces shortages of minerals and energy at home, is staging a worldwide search for outside investment sources.

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People used to talk about being "as rich as the Aga Khan." But no more. The Aga now has his troubles. The Aga (son of fabled Ali Khan) bought a series of 36 luxury hotels (the famous Ciga chain)

located throughout Europe. Unfortunately, luxury has not done well. Hotel rooms at $300 to $500 and up are just not in demand in the recessionary Europe of today. Also, over the past nine months the lira has lost 40% of its value against the dollar. Two weeks ago the Milan exchange halted trading in the Aga Khan's companies. Said a broker on the Milan exchange, "The Aga Khan made a series of bad decisions in recent years . . . and now he is paying the price."

GOLD, PRECIOUS METALS: So far, there doesn't seem to be any great excitement generated by the rise in precious metals. But let's face it, we really shouldn't expect any excitement -- the media and the public (they're the ones who would reflect the excitement) are always oblivious of the big (changing) picture.

At this point gold is somewhat overbought -- a little too much enthusiasm generated from gold-philes. In gold trading, the 20 dollar increments (i.e., 340, 360, 380) and the big 100 numbers (i.e., 300, 400, 500) have always been important. Therefore, the best action from here would be for gold to bounce around the 380-400 level -- then somewhere in the next few months or so push decisively above 400.

I have emphasized that this is the early, erratic, difficult part of the gold bull market. Gold at this point is going against powerful deflationary forces in the economy. But gold is looking ahead -- to the point where inflation will HAVE TO be substituted for deflation.

Again, remember my repeated warnings that in view of the massive amount of debt in the US, there are only two alternatives -- *"Inflate or die."* And believe me, politicians aren't going to choose death (deflation), they are going to chose inflation. The M-1 money supply, the adjusted monetary base, and adjusted reserves are all rising at double digit rates. The Fed may be talking caution but they are acting "pump, pump."

I've been saying that the rise in precious metals is VERY SIGNIFICANT. The advance is not merely a pop which will be over in a month or two. As I see it, the advance represents the early part of a tidal force, a primary switch from financial assets to real or tangible assets. And gold is its leader, its bellwether.

The primary trend is the single most difficult trend for the public to comprehend or accept. It's difficult to accept because the primary trend is a great unseen force. The primary trend is not based on a single news item or the consensus opinion of Wall Street analysts. The primary trend is always based on some basic condition which is the opposite of what the public and the media perceive.

"C'mon," said one commentator, "gold has been down so long that we have to consider the current rise as a blip, just a bounce in a long-running bear market. There's no reason to buy gold here. I've watched it for years, and every rally since 1980 has been followed by still lower prices."

You see, the above commentator is convinced that the past will be prologue, that nothing changes. For bulls on gold, that's exactly the kind of sentiment you want. The longer the public holds off buying gold and the longer and more intense the skepticism -- the greater and more dynamic will be the bull market in gold and the precious metals.

Bull markets have a habit of pushing higher until the public accepts them, embraces them, dives into them "hook, line and sinker." That's what's happening in the bull market in stocks. And in time it will happen in the precious metals markets as well.

Kemper Securities has issued a very interesting study on precious metals and the primary trend in the precious metals. *Kemper* identifies six "reflationary periods" in which the precious metals rose. These six periods are: (1) June 1967 to April 1969, 98 weeks duration; (2) May 1972 to January 1975, 139 weeks duration; (3) March 1977 to December 1980, 197 weeks duration; (4) September 1982 to October 1983, 59 weeks duration; (5) January 1986 to January 1988, 108 weeks duration; (6) the current period which *Kemper* states as having started in May 1993.

The average reflationary period (rising precious metals prices) was 120 weeks. If the current reflationary period was equal to the shortest previous period, it will end in June 1994. If it was to equal the longest period it would last until January 1997.

My own feeling is that this is a real, bona fide resumption of the bull market that began from the 1985 lows. It should develop into a MAJOR, EXTENDED bull market in the precious metals.

Because of the current high unemployment rate, I believe the Fed will be very reluctant to push rates up. In fact, if the US economy starts to accelerate on the upside, the Fed will breathe a sigh of relief. The attitude at the Fed, I believe, would be to let the economy run. That too will be a plus for gold. Remember the unspoken deal that Greenspan made with Clinton. Cut the deficit and we'll take care of the monetary situation. There will be no shortage of money. The Fed is clearly playing ball with Bill Clinton. Tie that in with the favorable supply/demand situation in gold and you have all the elements needed for a big bull market in the precious metals.

I'm receiving a ton of questions about gold and about investing in gold. The coins -- where do you buy them? Pick up your telephone book and check your local dealers. Call three or four and check for competitive prices. Then take possession of the coins. Put them in your bank vault or hide them in your attic, but be sure you remember where you hid them. One subscriber back in the '80s buried his coins in his backyard, then sold the house and forgot to retrieve his coins. The poor fellow had to sneak back one night and dig up his coin hoard. Luckily, he wasn't shot by the new home owners.

Here are some no-load gold mutual funds: Benham Gold Equities Index -- (800) 321-8321 or (415) 965-8300; Financial Strategic Gold Portfolio -- (800) 525-8085; Lexington Gold Fund -- (800) 526-0056 or in NJ (800) 932-0803; US Gold Shares Fund -- (800) 873-8637.

Gold futures are OK if you are very knowledgeable about commodities, which most of my subscribers are not. Remember, when you buy a future you are immediately locked into the price, regardless of whether the price of gold goes up or down. And you are subject to a time limit.

As for options, they are a lot more expensive now than when I first recommended the December 400s at ninety cents to one dollar (which meant paying $100 for an option that gave you a call on 100 ounces of gold at $400 an ounce). Those options last week rose to 17 or $1,700 an option. Yep, you can make money in options, but the time to buy options are (1) when they are cheap, meaning when nobody wants them, and (2) when you're buying options on an item that nobody thinks is going anywhere. That was gold back in January-February. My opinion -- gold options are too expensive now.

Then there are the stocks, and for this see Investment Position.

LATE NOTES: What's happening in the market is becoming increasingly clear. As I've written many times before, **38%** of all the stocks on the NYSE are now extremely interest rate-sensitive (these include the numerous preferreds, the many bond funds, the banks stocks, the S&Ls, the brokerage stocks, etc.). With interest rates dropping persistently lower, this 38% of the market has been creeping higher. But under the guise of declining interest rates, a great many "regular" common stocks have been hit and hit hard. Thus, many portfolios holding a variety of common stocks (including top-grade issues) are now under water, and investors can't understand why (why, with the stock averages moving higher).

Is a bear market operating, hidden by the 38% of interest-sensitive stocks? I've been wondering about that, and it's making me very uneasy.

NEXT MAILING: August 4, 1993